

# LEGISLATIVE OPPOSITION TO CHAIN STORES AND ITS MINIMIZATION

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While less direct in their application than other types of legislation, chain store taxes are none the less marketing barriers in the broad sense in which the term is used in this symposium.<sup>1</sup> Their effect—indeed their avowed purpose—is to obstruct one channel of distribution in order to divert the flow of goods into other channels. This article discusses three phases of the subject: first, the history of chain store taxes and their treatment at the hands of the courts; second, other legislation with an anti-chain store “flavor,” such as the Robinson-Patman Act, fair trade laws, sales-below-cost laws, and state price discrimination laws; and third, some of the economic effects of the foregoing, including devices used for their minimization.

## CHAIN STORE TAXATION<sup>2</sup>

The first tax aimed at chain stores was a city ordinance of Danville, Kentucky, which provided for taxation of cash-and-carry stores at a higher rate than ordinary grocery stores. It was declared unconstitutional by the state courts in 1925 on the ground of improper tax classification.<sup>3</sup> In 1927, Maryland enacted a law levying a tax of \$500 per store on all stores in any chain consisting of six or more stores in Allegany County.<sup>4</sup> This was declared unconstitutional the following year<sup>5</sup> in an opinion interesting for its forecast of the development, almost a decade later, of the supermarket. Within the ensuing several years chain store taxes were enacted and declared unconstitutional in Georgia,<sup>6</sup> South Carolina<sup>7</sup> and North Carolina.<sup>8</sup>

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<sup>1</sup> Indeed, the Marketing Laws Survey of the Works Progress Administration included chain store tax laws in its *Digest of State Laws Relating to the Problem of Interstate Trade Barriers for States Whose Legislatures Convene in 1940* (Jan. 1940).

<sup>2</sup> For greater detail on various phases of the chain store tax movement, consult Becker and Hess, *The Chain Store License Tax and the Fourteenth Amendment* (1929) 7 N. C. L. REV. 115; Collins, *Anti-Chain Store Legislation* (1939) 24 CORN. L. Q. 198; Brown, *A Note on Federal Taxation of Chain Stores* (1940) 13 J. BUS. UNIV. CHI. 74; Lee, *Recent Trends in Chain-Store Tax Legislation* (1940) 13 *id.* 253.

<sup>3</sup> *City of Danville v. Quaker Maid Co.*, 211 Ky. 677, 278 S. W. 98, 43 A. L. R. 590 (1925).

<sup>4</sup> Md. Laws 1927, c. 554, §§1-3.

<sup>5</sup> *Keystone Grocery & Tea Co. v. Huster*, Circuit Court of Allegany County, Md., Apr. 21, 1928, Equity 10,922 (unreported).

<sup>6</sup> *F. W. Woolworth Co. v. Harrison*, 171 Ga. 891, 156 S. E. 904 (1931).

<sup>7</sup> *Southern Grocery Stores v. Query*, Court of Common Pleas, Richland County, S. C., Feb. 27, 1929 (unreported).

<sup>8</sup> *Great A&P Tea Co. v. Doughton*, 196 N. C. 145, 144 S. E. 701 (1928). The North Carolina

As can be seen, prior to 1931, chain store taxes were generally considered invalid. In that year, however, the United States Supreme Court handed down its well-known decision in *State Board v. Jackson*,<sup>9</sup> upholding an Indiana tax graduated from \$3 on one store to \$25 on each store in excess of twenty. Since this leading case precipitated the flood of chain store taxes now on the books of some twenty states, it is worth while to examine it briefly.

The case was tried before a statutory three-judge federal district court which, after hearing voluminous testimony on both sides, concluded that the act was unconstitutional. A direct appeal was taken to the Supreme Court of the United States. It so happened that during the trial of this case in the court below, Federal Equity Rule 70½ was not in effect and the district court made no findings of fact. Ordinarily the Supreme Court would have sent the case back for such findings, but in this instance decided to make its own factual summary. The evidence was conflicting and findings of fact in either direction were possible. The district court, being opposed to the tax, would probably have made findings on which a reversal could have been supported only with difficulty. Without necessarily challenging the ingenuity of the Supreme Court to surmount such an obstacle, the writer believes that had the district court done this, its decision might have been affirmed and the entire chain store tax movement nipped in the bud. As it was, the Supreme Court held that the possession by chain stores as a class of thirteen "advantages" over independent merchants justified their separate treatment for taxation.

Since the *Jackson* case the Supreme Court has on four occasions dealt with anti-chain tax enactments. *Fox v. Standard Oil Co.*<sup>10</sup> concerned the express inclusion of filling stations in a chain store tax ranging from \$2 on two stores to \$250 per store on more than 75 stores. As in the *Jackson* litigation a finding of invalidity by the lower federal court<sup>11</sup> was reversed on appeal. Twice has the Court dealt with the measure of per-store taxes. *Liggett v. Lee*<sup>12</sup> involved a rate schedule so constructed as to impose heavy additional taxes where the stores were located in more than one county.<sup>13</sup> The Court held the basic tax valid, but declared that classification of rates on the basis of county boundary lines was improper. In doing so, however, it indicated that, if properly set up, a greater tax might validly be levied on national as distinguished from local chains.

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law was later amended so as to provide a tax of \$50 on every store in a chain of two or more stores in the state, the former tax applying only if the chain owned six or more stores in the state. As amended, the North Carolina law was declared constitutional in *Great A&P Tea Co. v. Maxwell*, 199 N. C. 433, 154 S. E. 838 (1930), *aff'd* (after the *Jackson* case, *infra*), 284 U. S. 575 (1931).

<sup>9</sup> 283 U. S. 527 (1931).

<sup>10</sup> 294 U. S. 87 (1935).

<sup>11</sup> *Standard Oil Co. v. Fox*, 6 F. Supp. 494 (S. D. W. Va. 1934).

<sup>12</sup> 288 U. S. 517 (1933).

<sup>13</sup> This law also imposed a tax of \$3.00 on each \$1,000 worth of stock carried in chain stores and chain warehouses, as compared with a tax of only \$1.50 per \$1,000 on stocks of ordinary wholesalers. This discrimination was held valid. Also held valid was a provision in the law permitting counties and cities to impose chain store taxes equal to 25 percent of the state tax. In addition, the exemption of filling stations from this law was held valid on the ground that they constitute a distinct line of business which already pays heavy license and gasoline taxes.

Thus was foreshadowed the Court's later decision in *Great Atlantic & Pacific Tea Co. v. Grosjean*,<sup>14</sup> sustaining the Louisiana provision that the tax, though applied only to stores located within the state, was to be measured by the total number of units in the chain wherever located. In *Stewart Dry Goods Co. v. Lewis*<sup>15</sup> graduated gross receipts taxation of all retail merchants was judicially condemned. The Court's unfavorable view was grounded on the fact that the tax was not confined to a particular *method* of merchandising and was not justified by the proposition that profits increase with sales.<sup>16</sup>

So much for the decisions of the United States Supreme Court. Following their defeat in the *Jackson* case, the chain stores sought on a number of occasions to have chain store taxes declared invalid by state courts under their respective state constitutions. Until rather recently, however, this effort was unsuccessful.<sup>17</sup> In the past two years the chain stores have been more fortunate, and while their success is by no means phenomenal, it may mark a turning point in the attitude of the courts toward chain store tax legislation. In 1939, the courts of two states declared their chain store taxes to be in violation of the state constitution.<sup>18</sup> The first of these cases was *Great Atlantic & Pacific Tea Co. v. Kentucky Tax Commission*,<sup>19</sup> involving a tax graduated from \$2 on one store to \$300 on each store over fifty. In holding that this tax violated the state constitution the court stated that the statute could not be upheld as a police measure because on its face it was for revenue purposes.

<sup>14</sup> 301 U. S. 412 (1937).

<sup>15</sup> 294 U. S. 550 (1935).

<sup>16</sup> The decision in the *Stewart Dry Goods* case was followed in: *Tollerton & Warfield Co. v. State Board*, 222 Iowa 908, 270 N. W. 427 (1936); *State ex rel. Lane Drug Stores v. Simpson*, 122 Fla. 637, 166 So. 227 (1936); *State ex rel. Adams v. Lee*, 166 So. 249 (Fla. 1936); *Safeway Stores v. Vigil*, 40 N. M. 190, 57 P. (2d) 287 (1936); *Schuster & Co. v. Henry*, 218 Wis. 506, 261 N. W. 20 (1935), *cert. denied*, 296 U. S. 625 (1935); *Great A&P Tea Co. v. Harvey*, 177 Atl. 423 (Vt. 1935); *Great A&P Tea Co. v. Valentine*, 12 F. Supp. 760 (S. D. Iowa 1935), *aff'd*, 299 U. S. 32 (1936). In *National Tea Co. v. Minnesota*, 205 Minn. 443, 286 N. W. 360 (1939), the Supreme Court of Minnesota declared the graduated gross receipts tax of that state unconstitutional. The Supreme Court of the United States, on *certiorari*, uncertain whether the decision in the state supreme court was based on the state or federal constitution, sent the case back for clarification of this point. 309 U. S. 551 (1940). The state supreme court on Sept. 27, 1940, reconsidered the case and handed down an opinion stating categorically that the tax violated the uniformity clause of the state constitution.

<sup>17</sup> Chain store taxes were declared valid in the following cases: *Shyer's, Inc. v. Butler*, Circuit Court of Montgomery County, Ala., July 25, 1933 (unreported); *J. C. Penney Co. v. Diefendorf*, 54 Idaho 374, 32 P. (2d) 784 (1934); *C. F. Smith Co. v. Fitzgerald*, 270 Mich. 659, 259 N. W. 352 (1935); *Hurt v. Cooper*, 130 Texas 433, 110 S. W. (2d) 896 (1937). In addition the chain store tax in South Carolina was held valid by a federal district court in *Southern Grocery Stores, Inc. v. Tax Commission*, 55 F. (2d) 931 (E. D. S. C. 1932); and a Mississippi statute levying a gross receipts tax of  $\frac{1}{4}$  of 1 percent on retailers and chains of five stores or less, with an additional  $\frac{1}{4}$  of 1 percent on chains of more than five stores, was held valid in *Penney Stores v. Mitchell*, 59 F. (2d) 789 (S. D. Miss. 1932), *appeal dismissed*, 287 U. S. 672 (1932).

<sup>18</sup> Chain store tax laws of two other states were also invalidated in 1939 for technical defects in their enactment: *Vaughn & Ragsdale, Inc. v. State Board*, 109 Mont. 52, 96 P. (2d) 420 (1939) (defective enacting clause); *C. Thomas Stores Sales System, Inc. v. Boyle*, District Court, 4th Judicial District, Hennepin County, Minnesota, Sept. 26, 1939 (unreported) (embracing more than one subject; also certain exemptions held discriminatory). A chain store tax in South Dakota was invalidated in 1936 because the bill did not receive the required two-thirds majority vote in the legislature. *Barnsdall Refining Co. v. Welsh*, 64 S. D. 647, 269 N. W. 853 (1936). These, however, were merely temporary successes on the part of the chains which postponed, but did not eliminate, chain store taxes from the states concerned.

<sup>19</sup> 278 Ky. 367, 128 S. W. (2d) 581 (1939).

It indicated, however, that if a business needed regulating under the police power, it should be regulated and not taxed out of existence. The state constitution was held to require that classifications of persons for tax purposes be made on a natural and reasonable basis, and the classification of chain stores was found not to fall in that category.

The Kentucky court reviewed the cases in which chain store taxes had been upheld, as well as those prior to the *Jackson* case in which they had been invalidated. It stated that most of the cases sustaining these taxes had construed the uniformity provision of the state constitution as applicable only to *ad valorem* taxes on property, and not to license fees; and, further, that the statutes in these cases were enacted under the police power and not purely as revenue measures. The court pointed out that the cases upholding chain store taxes indicated that it was constitutional to discourage or even destroy chain stores. The constitution of Kentucky, however, had never been so construed, but on the contrary forbade license taxes which confiscated property or suppressed legitimate occupations. The court specifically found that the thirteen "advantages" of chain stores enumerated in the *Jackson* case were not peculiar to the chains as a class.

The second case in which a chain store tax was invalidated in 1939 was *American Stores Co. v. Boardman*.<sup>20</sup> This case involved a Pennsylvania statute levying a tax graduated from \$1 on one store or theater to \$500 on each store or theater in excess of five hundred. The decision of the state supreme court was based entirely upon one ground, namely, that the constitution of Pennsylvania does not permit graduated taxation, but requires that *all taxes* be uniform.

Although the state supreme court did not mention the *Jackson* case, the lower court devoted considerable attention to this and other chain tax decisions. It pointed out that the decisions of the United States Supreme Court on the subject were closely divided: two of them 5-4, two 6-3 and one 4-3. This court held it immaterial that graduated chain store taxes existed in twenty-one states and that a majority of them had been held constitutional. Declaring that voluntary chains operate in the same way, the court stated that the evidence before it did not bear out the conclusions arrived at by the United States Supreme Court in the *Jackson* case on the "advantages" of corporate chain stores. Moreover, it held that it was not justified in saying, as the United States Supreme Court did in the *Grosjean* case, that a tax may increase in proportion to the number of stores since the opportunities and powers of a chain become greater with size.<sup>21</sup>

In addition to state chain store tax statutes, the chains have also been burdened at times with various types of discriminatory municipal ordinances. Their attacks on these in the courts have, on the whole, been somewhat more successful than

<sup>20</sup> 336 Pa. 36, 6 Atl. (2d) 826 (1939).

<sup>21</sup> In addition to the foregoing cases, an amendment to the Tennessee chain store tax providing that out-of-state corporations must pay one and one-half times the tax paid by domestic corporations, was held void. *Great A&P Tea Co. v. McCanless*, Tenn. Chancery Court, Pt. II, Tenn., July 14, 1939 (unreported).

their attacks on state legislation. As stated earlier, a discriminatory tax levied by the City of Danville, Kentucky, against cash and carry stores was invalidated in 1925.<sup>22</sup> A similar ordinance of the City of Douglas, Georgia, was invalidated in 1935.<sup>23</sup> Chain store tax ordinances of the graduated "per store" type enacted by the cities of Hamtramck, Michigan, St. Louis, Missouri, and Columbus and Augusta, Georgia, were also declared invalid.<sup>24</sup> The score for the chains has not been perfect, however, for chain store tax ordinances have been held valid by the Supreme Courts of Oregon, Virginia and South Carolina.<sup>25</sup>

Brief mention should be made of the status of chain store tax laws today,<sup>26</sup> and also of the Federal chain store tax proposed by Congressman Patman of Texas. Chain store tax laws are now on the books of twenty states.<sup>27</sup> Of these, only four are of the so-called "Louisiana" type in which the tax on stores within the state is based upon the number of stores both within and without the state.<sup>28</sup> The remaining sixteen are of the regular, or "Indiana," type, with the exception of the Tennessee statute which is based on floor space.

The Patman Bill, first introduced in 1938 as H. R. 9464, was re-introduced in 1939 as H. R. 1. It has maintained this designation through successive re-introductions ever since. The bill originally provided for a graduated chain store tax ranging from \$50 per store on chains of less than 10 units up to \$1,000 per store on chains of more than 500 units, and provided that the foregoing rates should be multiplied by the number of states (including the District of Columbia) in which the chain operated. At the time of the hearings, in the spring of 1940, the bill was revised by cutting the tax in half in each bracket and by providing that the tax did not apply to chains of 50 stores or less operated in and from a single state or within a radius of 100 miles of a single city. The revised bill also provided that for seven years after the effective date of the act the multiplication of the tax by the number of states in which the chain operated would not apply so long as the chain did not increase the number or change the location of its outlets. In addition, Mr. Patman proposed an amendment striking out the exemption of filling stations and making them subject to the tax.<sup>29</sup>

<sup>22</sup> *City of Danville v. Quaker Maid Co.*, *supra* note 3.

<sup>23</sup> *City of Douglas v. South Georgia Grocery Co.*, 179 S. E. 768 (Ga. 1935).

<sup>24</sup> *Kroger Grocery & Baking Co. v. City of Hamtramck*, Circuit Court for the County of Wayne, Mich., Dec. 23, 1932 (unreported); *Kroger Grocery & Baking Co. v. St. Louis*, 341 Mo. 62, 106 S. W. (2d) 435 (1937); *Great A&P Tea Co. v. City of Columbus*, 189 Ga. 458, 6 S. E. (2d) 320 (1939); *Southern Grocery Co. v. City of Augusta*, 189 Ga. 618, 7 S. E. (2d) 181 (1940); *Great A&P Tea Co. v. City of Columbus*, Muscogee Superior Court, Aug. 27, 1940 (unreported).

<sup>25</sup> *Safeway Stores, Inc. v. City of Portland*, 149 Ore. 581, 42 P. (2d) 162 (1935); *City of Fredericksburg v. Sanitary Grocery Co.*, 168 Va. 57, 190 S. E. 318 (1937); *Great A&P Tea Co. v. Spartanburg*, 170 S. C. 262, 170 S. E. 273 (1933).

<sup>26</sup> As of December 1940. No new chain store taxes were, to the writer's knowledge, enacted during the first six weeks of 1941, although legislatures of forty-three states have been in session.

<sup>27</sup> Ala., Colo., Fla., Ga., Idaho, Ind., Iowa, Ky., La., Md., Mich., Minn., Miss., Mont., N. C., S. C., S. D., Tenn., Tex. and W. Va. The chain store tax of Wisconsin expired on July 1, 1940, by its own terms, and has not been re-enacted. The Kentucky statute was passed in 1940, notwithstanding the invalidation in 1939 of the prior law, for which see note 19, *supra*. <sup>28</sup> Ky., La., Miss. and S. D.

<sup>29</sup> *Hearings Before the Subcommittee of the Senate Committee on Ways and Means on H. R. 1*, 76th Cong., 3d Sess. (1940) 5.

Despite the reduction of the proposed tax by half, it was obvious that its purpose and effect was still to drive out of existence chains operating in more than one state. The Great Atlantic and Pacific Tea Company with approximately 9,000 stores located in 39 states would have to pay a tax under the original bill of over \$300,000,000 per year, yet its total sales in 1938 were only \$881,703,076 and its net profits \$9,119,114.<sup>30</sup> The tax under the original bill was over 30 percent of the Atlantic & Pacific Tea Company's total sales and nearly 33 times its net profits. Cutting the tax rate in half had about the same practical effect as reducing the prison sentence of a convict from 998 years to 499 years.

The seven-year moratorium on the multiplication feature of the tax was also of little benefit to large chains, for in order to avail themselves of it they had to refrain from adding any new stores or moving the locations of any existing stores. This prevention of natural expansion, and of such re-location as would be necessary to keep pace with the shifts of local business, amounted to slow strangulation.<sup>31</sup>

#### ANTI-CHAIN STORE "FLAVOR" OF OTHER LEGISLATION

Space does not permit more than brief consideration of such less direct anti-chain store legislation as the Robinson-Patman Act, state fair trade laws, sales-below-cost laws and state anti-discrimination laws.<sup>32</sup>

The Robinson-Patman Act<sup>33</sup> was enacted in 1936 largely at the behest of organized wholesale grocers and food brokers. In essential purpose it was an anti-chain store measure, designed to deprive the chains of purchasing advantages which the proponents of the act believed they had been getting. Briefly, the law provides that discriminations between purchasers are lawful only if justified by differences in the cost of manufacturing, selling, and delivering the goods to such purchasers. In addition, it prohibits the payment of brokerage in any form by a seller to a buyer under any circumstances.<sup>34</sup> The act also prohibits a seller from giving a buyer any services or facilities, or any payment for services performed by the buyer, unless made available to all buyers on proportionately equal terms. A buyer who know-

<sup>30</sup> *Id.* at 153.

<sup>31</sup> H. R. 1, 77th Cong., 1st Sess., as reintroduced in 1941, provides for a tax graduated from \$25 on chains of 15 stores or less up to \$500 on each store in excess of 500, the foregoing rates to be cut in half during the fiscal year following date of enactment, and to be cut one-fourth during the second such fiscal year. The multiplication of the tax by the number of states in which the chain operates is applicable only against such stores as are physically located in premises not occupied by a store of that chain on the effective date of the act (unless such premises were abandoned and later re-occupied by the same chain). It is provided that none of the provisions of the bill (including the basic tax as well as the multiplied tax) shall apply to chains of 50 stores or less located in and operated from a single state or within a radius of 100 miles of a single city, nor to any chain with a gross business of \$250,000 or less per annum.

<sup>32</sup> These laws formed the subject of an earlier symposium in this journal, *Price Discrimination and Price Cutting* (1937) 4 LAW & CONTEMP. PROB. 271 *et seq.*

<sup>33</sup> 49 STAT. 1528, 15 U. S. C. A. §13 (1936).

<sup>34</sup> Literally, the act permits the payment of such brokerage for "services rendered," but the courts have held that buyers cannot render services to sellers as a matter of law. *Great A&P Tea Co. v. Federal Trade Commission*, 106 F. (2d) 667 (C. C. A. 3d, 1939), *cert. denied*, 308 U. S. 625 (1940).

ingly induces or receives a discrimination prohibited by the act is equally liable with the seller.<sup>35</sup>

Fair trade laws are found on the books of forty-four states.<sup>36</sup> They provide in substance that a manufacturer may enter into contracts with his wholesale or retail dealers establishing the prices at which the latter are to resell the manufacturer's trademarked or branded merchandise. A contract with a wholesaler may also provide that when the wholesaler resells to a retailer he will require the retailer to enter into a similar contract. Such contracts are expressly exempt from the state anti-trust laws.<sup>37</sup> The fair trade laws also provide that whenever any such resale price contracts are in effect with respect to a manufacturer's product no person, whether a party to the contract or not, shall wilfully and knowingly advertise, offer or sell that product at less than the contract price. Thus by entering into a contract with a single dealer, and sending notices of it to all other dealers, a manufacturer can effectively peg resale prices on his product throughout the entire state. These laws have been held constitutional by the United States Supreme Court.<sup>38</sup>

So-called sales-below-cost laws are found on the books of twenty-six states.<sup>39</sup> These laws vary considerably in detail, but in general prohibit retailers and wholesalers<sup>40</sup> from selling at less than invoice or replacement cost (whichever is lower) plus the cost of doing business. Some of these laws define "cost of doing business" in very broad terms, and state that cost surveys made with respect to a particular trade in a particular locality shall be deemed competent (or *prima facie*) evidence of such cost. Others establish a specific percentage mark-up (frequently 6% for retailers and 2% for wholesalers) as the "cost of doing business." The mark-up applies only in cases where the wholesaler or retailer cannot prove a lower cost of doing business. Virtually all of these laws prohibit sales below cost only when made with the intent or effect of injuring competitors or destroying competition. They do not apply in certain enumerated cases, such as sales of perishable articles to forestall loss, sales of discontinued lines, sales under court order, sales to meet a competitor's price, and the like.

State anti-price discrimination laws are found on the books of twenty-five states,

<sup>35</sup> Other provisions of the act are: (a) A criminal provision prohibiting price discrimination, locality price discrimination, and sales at "unreasonably low prices," which has never been enforced. (b) A provision dealing with litigation pending under the original Section 2 of the Clayton Act at the time the Robinson-Patman Act was passed. (c) A provision exempting from the act the payment of patronage dividends by co-operatives to their members. (d) An amendment providing that the act does not apply to purchases by schools, colleges, universities, public libraries, churches, hospitals and charitable institutions not operated for profit.

<sup>36</sup> All states except Del., Mo., Tex. and Vt.

<sup>37</sup> The Tydings-Miller Act, 50 STAT. 693, 15 U. S. C. A. §1 (1937), grants a similar exemption from the Sherman Act with respect to resale price maintenance contracts on goods which are to be resold in a state where such contracts are made lawful by any statute, law or public policy. This removes the danger of entering into Fair Trade contracts in connection with interstate commerce. Previously such contracts violated the Sherman Act. *Dr. Miles Medical Co. v. Parks*, 220 U. S. 373 (1911).

<sup>38</sup> *Seagram Distillers Corp. v. Old Dearborn Distributing Co.*, 299 U. S. 183 (1936).

<sup>39</sup> Ariz., Ark., Cal., Colo., Conn., Idaho, Ky., La., Me., Md., Mass., Mich., Minn., Mont., N. J., Ore., Pa., R. I., S. C., Tenn., Utah, Va., Wash., W. Va., Wis., Wyo.

<sup>40</sup> A few of them also prohibit sales below cost by manufacturers.

often in combination with a sales-below-cost law.<sup>41</sup> These laws fall into two classes. Those in three states are patterned upon the Federal Robinson-Patman Act.<sup>42</sup> The rest merely prohibit the sale of goods by a person at one place in the state at a lower price than in another place for the purpose of injuring competitors or destroying competition. The origin of some of these laws goes back to the early part of this century. Their original purpose was to prevent a monopolistic practice prevalent at that time in which a large combination, seeking to gain control of the market, cut prices in one locality until its competitors were driven out of business, meanwhile maintaining higher prices in localities where no competition existed.

The attempt to apply these laws to chain stores is of recent origin and thus far has not fared well at the hands of the courts.<sup>43</sup> It has generally been demonstrated that where a chain sells at different prices in its different stores, it does so not for the purpose of injuring competition or creating monopoly, but for the purpose of meeting local competitive conditions or of reflecting differences in the cost of operations at different store locations.

#### ECONOMIC EFFECTS AND MINIMIZATION OF ANTI-CHAIN LEGISLATION

It is impossible to discover with precision the effects of any of the foregoing laws, including chain store taxes, upon the economy. The writer is not aware of any statistical surveys showing whether or not chain store taxes have caused a direct price increase to consumers. That their *purpose* lies in this direction cannot be questioned, but it is not at all clear that this purpose has been fulfilled.

Although a chain may decide to absorb the tax and take a smaller net profit, the burden of the tax may cause it to curtail existing or proposed operations which would otherwise be profitable and, by cutting down total volume, increase costs of operation. It is undoubtedly true that chain store executives have refrained from opening stores that would have been opened had there been no chain store tax. This is particularly true of experimental stores opened in growing neighborhoods to take advantage of a good location before the business in the neighborhood actually reaches its full growth. It was quite a common practice in the past to open such stores and to operate them, not at a loss, but at a lower rate of profit than was ultimately to be expected. This practice has undoubtedly been cut down severely by the existence of chain store taxes.

On the other hand, it cannot be said that all chains have suffered a loss of volume with consequent higher operating costs as a result of chain store taxes. The development of the supermarket has in large measure prevented this. Where a chain has gone into the supermarket type of operation on a sizeable scale, it is the writer's opinion that chain store taxes have not produced an increase in prices. And it is

<sup>41</sup> The following states have anti-discrimination but not sales-below-cost laws: Fla., Iowa, Kan., Miss., Mo., Neb., N. D., Okla., S. D. The following states have sales-below-cost laws but not anti-discrimination laws: Ariz., Conn., Me., Md., N. J., Pa., R. I., Tenn., Va. and W. Va. All of the other states listed in note 39, *supra*, have both types of laws.

<sup>42</sup> Idaho, Ore., Utah.

<sup>43</sup> Great A&P Tea Co. v. Ervin, 23 F. Supp. 70 (D. Minn. 1938).



doubtful whether chains that have not entered the supermarket field have been able to increase prices either, in view of the necessity of meeting competition. On the whole, therefore, it is probable that the effect of the taxes on chains in the latter category has been to reduce profits.

In this connection, two tendencies in the evolution of chain store taxes since the *Jackson* case should be noticed. First, the amount of the tax in the higher brackets has been greatly increased. The original Indiana law levied a maximum tax of only \$25 per store. Recent statutes have levied high tax rates, in Texas \$750 per store in the top bracket, and a number of municipal chain store taxes in Georgia were graduated as high as \$1,200 per store.<sup>44</sup> Secondly, the tax brackets have been progressively narrowed until the higher taxes fall upon smaller and smaller chains. Earlier laws levied their maximum rates only upon chains of several hundred stores, but a large number of the more recent statutes place extremely heavy taxes on purely local chains of as little as 20 stores. The Texas tax of \$750 per store applies to chains of 51 stores and over. It may well be questioned how far these two tendencies will run before reaction sets in. The decisions of the United States Supreme Court indicate that the Federal Constitution would not forbid a tax so heavy as to drive chains out of business entirely,<sup>45</sup> but it seems doubtful that state legislatures will be willing to go that far. As heavier and heavier taxes are applied, particularly in the lower brackets, political repercussions will be heard. Taxes of this type discourage even the progressive local merchant from expanding his business.

While it might at first appear that taxes on very large chains could be increased to confiscatory levels without political hazard, the psychology of the purchasing public must be kept in view. The average housewife has a two-cell mind on the chain store question. She may swallow a good deal of anti-chain propaganda as an academic matter, but she will continue to buy her groceries at the chain store because of its lower prices. To date, she has been able to view chain store taxes with apathy, for she has yet to encounter or realize any substantial effects upon her buying habits. If the chains should begin to disappear from the community, however, theories would very likely be rejected in favor of the compelling requirements of the home budget, and a broad change in public feeling might well take place. Such an awakening would be quickened and enhanced by the rather recent activities of the chains in presenting their side of the case to the consumer. For years these organizations did little or nothing to counteract the flood of propaganda against them, hoping perhaps that economic virtue would triumph unaided. They have realized, however, that pressure groups thrive on public apathy, and that an aroused consumer is their best safeguard.

Pressure groups that are too successful usually end by going too far and destroying all that they have accomplished. The anti-chain store campaign seems well along this road. In an attempt to extend their gains, the wholesale and retail

<sup>44</sup> These, however, were declared unreasonable and invalid. See note 24, *supra*.

<sup>45</sup> "When the power to tax exists, the extent of the burden is a matter for the discretion of the lawmakers." *Fox v. Standard Oil Co.*, *supra* note 10, at 99.

merchants who are behind the movement are alienating many of their own number—persons who formerly backed, or at least did not oppose, chain store legislation. Illustrative of this tendency is a bill introduced this year in the legislature of South Dakota levying a license tax of \$10 on separate grocery stores or butcher shops, but a tax of \$1,000 on stores selling both groceries and meats in combination.<sup>46</sup> More important, however, has been the gradual encroachment of chain store taxes upon voluntary chains. These chains are nothing more than groups of independent merchants, each owning his own store but banded together for the purpose of co-operative buying, joint advertising, uniform store fronts and methods of merchandising, and greater efficiency. The voluntary chain is the progressive independent merchant's answer to chain store competition.

Voluntary chains fall into two classes: first, retailer-owned co-operatives in which the retail members of the organization own their central warehouse; and, second, wholesaler-sponsored organizations in which the retailers enter into an arrangement with an existing wholesaler to purchase supplies through him on a co-operative basis and to follow common merchandising methods. Although, to the writer's knowledge, chain store taxes have not yet been applied to any of the large well-known voluntary or co-operative chains, the time when this will be done is fast approaching. The courts have already held these taxes applicable to organizations very similar in their characteristics.

In *Bedford v. Gamble-Skogmo, Inc.*<sup>47</sup> the question was raised whether so-called agency stores for the sale of automobile accessories were controlled by the company under whose auspices they were set up. The Gamble-Skogmo Company operated under its direct ownership a chain of automobile accessory stores which it conceded to be subject to the tax. It contested the application of the tax, however, to a group of independently owned stores which were operated under contract with it. These stores were colored and maintained in the same uniform style as the company's own stores. They used advertising furnished by the company. The company suggested their methods of bookkeeping, accounting, and sales and credit operations. The stores sold the goods of the company almost exclusively, and replaced defective merchandise of the company whether sold by them or some other agency or company store. The arrangement between the company and the agency was cancellable by either party on thirty days' notice, at which time the company had an option to buy up the merchandise and fixtures and take over the lease on the agent's location.

The Colorado court held that the object of this arrangement was to reap the advantages of chain store operation without assuming its burdens, and held that

<sup>46</sup> S. D. H. B. 122, 1941. For analysis of legislation of this character consult Cook, *Legislative Restrictions on Marketing Integration*; Edwards, *Economic Implications of Business Boundary Laws*, both *supra* this issue.

<sup>47</sup> 105 Colo. 424, 91 P. (2d) 475 (1939). See also a similar case in which the same decision was reached under the Idaho chain store tax. *Idaho v. Gamble-Skogmo, Inc.*, Dist. Court, 3rd Judicial District, County of Ada, June 12, 1940 (unreported). But *cf.* *Ford Motor Company v. Armstrong*, Colo. Dist. Court, City and County of Denver, Feb. 9, 1940 (unreported) in which it was held that Ford dealers were not "controlled" by the Ford Motor Company and hence not subject to the chain store tax.

the agency stores were "controlled" by the company and hence subject to the chain store tax. In passing, the court distinguished this agency arrangement from a voluntary co-operative chain by pointing out the absence of mutuality and of joint control by the members of the group. However, it seems to the writer that the arrangement between Gamble-Skogmo, Inc., and its agency stores was practically identical with the arrangement commonly found in a wholesaler-sponsored voluntary chain in the grocery field, and that on the basis of this decision such voluntaries could be subjected to chain store taxes.

Of significance also is *Belk Bros. v. Maxwell*.<sup>48</sup> This case concerned 46 stores, each of which was a separate corporation. None of the corporations owned stock in any of the others. The plaintiff (Belk) owned some, but less than a majority, of the stock in each corporation. He participated in the organization of all of them, and was the president and a member of the board of directors of each. The other directors were not interlocking in any respect. The stores all operated under the name of Belk. Their accounts were audited by the plaintiff at their expense, and they maintained a joint buying office in New York. The North Carolina court held that this group of stores constituted a chain within the meaning of the act and that they possessed the thirteen "advantages" of chain stores, enumerated in the *Jackson* case. The court further held that the application of the tax to this type of operation did not render it unconstitutional, stating that while the Supreme Court had pointed out the distinction between voluntary and corporate chains in *Liggett v. Lee*,<sup>49</sup> it had not held that taxation of the former would be improper.<sup>50</sup>

It may well be wondered whether the proponents of chain store legislation will be able to maintain their political strength and effectiveness if they alienate so large and powerful a group of strictly local independent merchants as the voluntary chains. Mr. Hector Lazo, head of the National Retailer Owned Grocers' Association, a national organization of co-operative chains, not long ago said: "A law passed today to put your competitor out of business may whack you between the eyes tomorrow."<sup>51</sup>

The minimization of chain store taxation through various devices designed to place the chain outside the scope of the law has been only partially successful. A typical device was the lease-and-license arrangement under which major oil companies established filling stations. By this arrangement, which is generally referred to as the "Iowa Plan," the oil company, either owning or leasing the filling station property, leased or sub-let it to an independent operator and entered into a contract with him to market the oil company's products. The details of the various contracts differed in individual cases, sometimes rather widely, and space does not permit discussing them. Suffice it to say that of six cases on the subject, only one held that the independent leased stations were not subject to the tax,<sup>52</sup> while five held that they were subject to the tax.<sup>53</sup>

<sup>48</sup> 215 N. C. 10, 200 S. E. 915 (1939).

<sup>49</sup> *Supra* note 12.

<sup>50</sup> See also *Southern States Fredericksburg Service v. Fredericksburg, Corporation Court of the City of Fredericksburg, Va.*, Aug. 6, 1940 (unreported).

<sup>51</sup> *Chicago Daily News*, June 22, 1939.

<sup>52</sup> *Standard Oil Co. v. Green*, 34 F. Supp. 30 (S. D. Iowa 1940).

<sup>53</sup> *Standard Oil Co. v. Texas*, 142 S. W. (2d) 519 (Tex. Civ. App. 1940); *Standard Oil Co. v. State*

In addition to attempting to eliminate their leased stations from the tax, a number of the oil companies tried to show that filling stations were not "stores" within the meaning of chain store tax statutes. This contention, if upheld, would have eliminated from the tax not only the leased stations but the company-owned stations as well. However, in only one case, to the writer's knowledge, was the contention of the oil companies upheld.<sup>54</sup> In three cases, filling stations were definitely held to be "stores" within the meaning of the statutes.<sup>55</sup>

Insofar as ordinary chains are concerned, the only significant attempt made to minimize chain store taxes was by cutting down on the number of stores. This was accompanied by a tendency to replace the closed stores with units doing a large volume of business. Thus, chain store taxes are, in part at least, responsible for the development of the supermarket. It is doubtful, however, that chain store taxes were the sole cause of this development. On the contrary, it is generally conceded that the first supermarkets were independent stores. One writer claims that the supermarket was born in Los Angeles, California, as early as 1925 in the form of "drive-in-markets," which were simply parking spaces with a row of small stores and restaurants. The idea did not work, but out of it came the principle of the supermarket which commenced its growth in 1929. According to this writer, the first Eastern supermarket was opened in a garage on Long Island in August, 1930. The famous Big Bear was opened in a vacant automobile plant in Elizabeth, N. J., in 1932.<sup>56</sup>

These were all independent stores and were set up at a time when the chains were still operating on a small neighborhood service store basis. The competition from the supers was keen and eventually the chains would have had to meet it regardless of chain store taxes. That the increased pressure of these taxes spurred the movement along cannot be questioned, and it is probably true that some chain store companies entered the supermarket field solely for the purpose of minimizing their tax burden. It is generally conceded by now, however, that the supermarket has proved so efficient and profitable a method of merchandising that it would undoubtedly remain even if all chain store taxes were repealed.

The sponsors of anti-chain legislation, seeing in the supermarket a new menace to their existence, have made sporadic attempts at legislation against this type of store. They were successful in having ordinances enacted in several cities in New Jersey levying a tax of \$200 on every concession or department rented, leased or operated, in any market in which food is sold. These taxes have been upheld by the courts.<sup>57</sup> However, taxes of this kind apply only to a special type of market in

Board, 99 P. (2d) 229 (Mont. 1940); *Maxwell v. Shell Eastern Petroleum Co., Inc.*, 90 F. (2d) 39 (C. C. A. 4th, 1937); *Gulf Refining Co. v. Fox*, 297 U. S. 381 (1936); *Mid-Western Petroleum Corp. v. State Board*, 206 Ind. 688, 187 N. E. 882 (1933).

<sup>54</sup> *Wadhams Oil Co. v. State*, 210 Wis. 448, 245 N. W. 646 (1932).

<sup>55</sup> *Fox v. Standard Oil Co.*, *supra* note 10; *Fox v. Gulf Refining Co.*, 295 U. S. 75 (1935); *Mid-Western Petroleum Corp. v. State Board*, *supra* note 53.

<sup>56</sup> Davidson, *What About Supermarkets?* (Sept. 17, 1938) 211 SAT. EVE. POST 23.

<sup>57</sup> *Giant Tiger Corp. v. City of Camden*, 122 N. J. L. 240, 4 A. (2d) 775 (1939); *American*

which the owner operates only the grocery department and leases out concessions in which all kinds of merchandise are sold. These are really department stores of a unique type and quite different from the exclusive grocery supermarket operated by chain store companies.

An attempt to legislate against the latter type of market has been made in Camden, Atlantic City, and several other communities in New Jersey. Ordinances were passed levying a tax as high as \$10,000 per year on any store operated on a self-service basis. The type of store covered by the ordinance was defined in considerable detail, specific mention being made even of the baskets used in accumulating merchandise prior to checking it out and paying for it. However, these ordinances have been declared unconstitutional in the case of *Great Atlantic & Pacific Tea Co. v. Camden*.<sup>58</sup> The court found that self-service methods of merchandising had long been in vogue and that fundamentally, except for the use of baskets, there was no difference between the stores subject to the tax and those not subject to it. A tax of \$10,000 a year for the use of so common an article as a market basket was held to be unreasonable.

A brief word about the economic effects of the Robinson-Patman Act and sales-below-cost laws will conclude this article.<sup>59</sup> The Robinson-Patman Act has unquestionably eliminated some of the purchasing advantages of large buying organizations, but it has by no means eliminated them all. As pointed out, the act permits price differentials reflecting savings in the cost of manufacturing and in selling the goods to particular buyers, and there is considerable doubt in the writer's mind whether the price differentials enjoyed by chains were ever in excess of these savings in the long run. In the practical application of the Robinson-Patman Act it is frequently possible for small wholesalers to obtain larger discounts than chain stores, chiefly because of the fact that small companies are less likely to be attacked by the Federal Trade Commission than are larger ones. This is not intended as a reflection on the Commission's policy of enforcement, which the writer knows to be completely fair. But the Commission cannot in the nature of things uncover all of the sporadic instances of price discrimination that may occur throughout the country. It simply does not have a large enough staff of investigators. The big chain, being in the limelight, cannot run the risk of violation, while the little wholesaler can afford to take a chance.

The Robinson-Patman Act has definitely eliminated the practice of paying brokerage to buyers, at least insofar as the corporate chains are concerned. Cases are still pending against some of the large voluntary chain organizations to force them also to discontinue the acceptance of brokerage. The brokerage section of the

Grocery Co. v. New Brunswick, 124 N. J. L. 293, 11 A. (2d) 599 (1940); Giant Tiger Corp. v. Trenton, 113 N. J. L. 34, 172 Atl. 565 (1934). <sup>58</sup> 122 N. J. L. 47, 4 A. (2d) 16 (1939).

<sup>59</sup> It would be beyond the scope of this article to discuss the economic effect of the fair trade laws. The subject is discussed rather thoroughly in a memorandum recently issued by the Department of Justice advocating the repeal of the Tydings-Miller Act (Feb. 10, 1941). In view of the fact that the state anti-discrimination laws have been largely ineffective, there is little need for discussion of their operation.

act has proved, however, a boomerang against the very group that sponsored it. As interpreted by the courts, this section prohibits any buyer from accepting brokerage. It has been a common practice of ordinary brokers to purchase an occasional car of merchandise on their own accounts for resale to their customers, but when they do this they cease to be brokers on that transaction and become buyers. The Federal Trade Commission has issued a large number of complaints and cease and desist orders against the practice of brokers purchasing on their own accounts and receiving commissions. Obviously, without such commissions, the broker cannot resell the merchandise at a profit and will, therefore, be forced to abandon this phase of his business. If this is a bad bed, however, it is one of his own making.

State sales-below-cost laws, if set up on a reasonable basis and not abused, have no discernibly harmful economic effects in the opinion of this writer. They have not generally been opposed by the chain stores, since the majority of chains disapprove of loss-leader selling and do not engage in the practice.<sup>60</sup> The trouble with state sales-below-cost laws has been the tendency of organized groups to misuse them by attempting, under their guise, to fix prices at levels having nothing to do with cost. Such abuses are most frequent where the law establishes no statutory mark-up above the cost of the goods, but permits "cost surveys" to be introduced as *prima facie* evidence of the cost of doing business. Cost surveys have been conducted in some states in a most informal manner, frequently by a mere vote of an interested group as to what the cost should be. In some states the "cost" established by these surveys has been raised progressively year by year until it has reached decidedly uneconomic levels. The Department of Justice recently secured indictments against a group of wholesalers and retailers in the State of Colorado for allegedly thus misusing that state's sales-below-cost law,<sup>61</sup> and investigations with an eye to similar indictments are now under way in a number of other states. If and when the abuses of the sales-below-cost acts are eliminated, and the laws themselves written on a reasonable basis with a mark-up that will not penalize the consumer, these laws should, on the whole, be beneficial in their effects.

#### CONCLUSIONS

In the writer's opinion, the events of the past few years indicate that the anti-chain store forces have pressed their advantage too far. Already a reaction has set in in the thinking of the courts; the public is beginning to get less of a one-sided picture; the abuses of legislation obtained by the anti-chain forces have come under attack by the Department of Justice; and the Federal Government as a whole has become aroused over the multiplication of interstate and other forms of marketing barriers. In the face of this, it seems inevitable that a reaction will ultimately take place in the state legislatures and result in the elimination of a great deal of the chain store legislation now on the books.

<sup>60</sup> *Hearings, supra* note 29, at 741-747.

<sup>61</sup> Department of Justice press release, Jan. 29, 1941.